



AUDITOR - GENERAL
SOUTH AFRICA

The Municipal manager
Umjindi Local Municipality
P. O. Box 33
Barberton
1300

Date: 30 November 2013

Reference: 02054REG12/13

Dear Sir

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Umjindi Local Municipality for the year ended 30 June 2013

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA)
2. We have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(3) municipality you are required to include the audit report in the municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.

6. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.
7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed


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Bomkazi Bhobho

Deputy Business Executive: Mpumalanga Business Unit

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REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE UMJINDI LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Umjindi Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Accumulated surplus

6. I was unable to obtain sufficient appropriate audit evidence for prior year error adjustments amounting to R6 996 471 disclosed in the statement of changes in net assets. The municipality's records did not permit the application of alternative procedures. In addition, a qualified opinion was issued on the prior year's financial statements. Consequently, I was unable to determine whether the accumulated surplus was fairly stated.

Property, plant and equipment

7. Due to the qualified opinion issued on the prior year's financial statements, I was unable to determine the extent of the effect of these limitations on the closing balance of property, plant and equipment disclosed in the statement of financial position.

Assets

8. The municipality did not recognise all properties controlled by the municipality in accordance with the GRAP *Framework for the preparation and presentation of financial statements*. Properties amounting to R193 617 542 owned by the municipality were not recognised in the municipality's records. As a result, assets are understated by R193 617 542. Due to the limitation on the scope of my audit, I was unable to determine how these properties should have been classified in the financial statements. I was unable to confirm this by alternative means.

Investment properties

9. The municipality did not recognise all property held to earn rentals or for capital appreciation as investment property in accordance with GRAP 16, *Investment property*. Properties amounting to R8 813 035 owned by the municipality were not recognised in the municipality's records. As a result, investment property is understated by R8 8813 035 .
10. The municipality transferred properties amounting to R20 470 091 from investment properties to property, plant and equipment. I was unable to obtain sufficient appropriate audit evidence for the reason for the reclassification of the properties. I was unable to verify this through alternative procedures.
11. Due to the qualified opinion issued on the prior year's financial statements, I was unable to determine the extent of the effect of these limitations on the closing balance of the investment properties disclosed in the statement of financial position.
12. Consequently, I was unable to determine whether investment properties amounting to R76 140 100 were fairly stated.

Provisions

13. Due to the qualified opinion issued on the prior year's financial statements, I was unable to determine the extent of the effect of these limitations on the closing balance of the provision disclosed in the statement of financial position.

Value-added tax (VAT) payable

14. I was unable to obtain sufficient appropriate audit evidence to support prior period adjustments amounting to R7 109 684 processed for the VAT payable. I was unable to confirm this by alternative means. Consequently, I was unable determine whether the VAT payable amounting to R3 214 096 as disclosed in note 20 to the financial statements was fairly stated.

Assets for no consideration

15. GRAP 3, *Accounting policies, estimates and errors* requires an entity to correct material prior year errors by retrospective restatement. The municipality did not correct the prior year error relating to unrecognised investment properties amounting to R47 130 000 by restating prior year investment properties and the accumulated surplus.

Unauthorised expenditure

16. The municipality did not disclose unauthorised expenditure in the notes to the financial statements, as required by section 125(4) (a) of the MFMA. The municipality incurred unauthorised expenditure amounting to R6 668 709, due to overspending of the votes. Unauthorised expenditure is therefore understated.

Irregular expenditure

17. The municipality did not disclose irregular expenditure in the notes to the financial statements, as required by section 125(4)(a) of the MFMA. The municipality incurred irregular expenditure amounting to R18 311 690, due to supply chain management (SCM) processes not having been followed. Irregular expenditure as disclosed in note 45 to the financial statements is therefore understated.

Aggregation/Accumulation of immaterial uncorrected misstatements

18. The financial statements as a whole are materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following elements making up the statement of financial position, the statement of financial performance and the notes to the financial statements:

Statement of financial performance

- Revenue reflected as R216 157 763 is understated by R176 378
- Employee costs reflected as R63 741 309 are overstated by R2 126 345
- Repairs and maintenance reflected as R2 890 575 are overstated by R59 406
- General expenditure reflected as R52 657 162 is understated by R1 932 923
- Allowance for impairment reflected as R14 907 973 is understated by R2 364 241
- Impairment of property, plant and equipment reflected as R1 688 194 is overstated by R1 688 194
- Fair value adjustments: investment properties reflected as R29 837 900 are understated by R2 540 440
- Depreciation reflected as R25 431 201 is understated by R392 189

Statement of financial position

- Staff leave reflected as R4 673 882 is overstated by R354 598
- Property, plant and equipment reflected as R725 298 623 is understated by R2 080 383

- Provisions reflected as R10 565 218 are overstated by R1 686 898
- Receivables reflected as R25 852 350 are overstated by R 2 479 391
- Investment property reflected as R29 837 900 is understated by R2 540 440
- Trade payables reflected as R16 296 561 are understated by R1 497 140

Qualified opinion

19. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Umjindi Local Municipality as at 30 June 2013 and its financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

20. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

21. As disclosed in notes 39 and 40 to the financial statements, the corresponding figures for 2012 have been restated as a result of an error discovered during 2013 in the financial statements of the municipality at, and for the year ended, 30 June 2012.

Material losses

22. As disclosed in note 46 to the financial statements, material losses were incurred as a result of electricity and water losses.

Material impairments

23. The municipality impaired consumer debtors of R14 907 973 at 30 June 2013 that had been outstanding for more than 12 months. The recoverability of these amounts is doubtful.

Unaudited supplementary schedules

24. The supplementary information provided on page xx is not clearly differentiated from the audited financial statements. Management did not change the manner in which the unaudited supplementary information is presented, as requested.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

25. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

26. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages xx to xx of the annual report.

27. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability.
28. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
29. The reliability of the information in respect of the selected development priorities is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
30. The material findings are as follows:

Usefulness of information

Presentation

31. The National Treasury's *Guide for the preparation of the annual report* requires that explanations for variances between the planned and reported (actual) targets should be provided in all instances and should also be supported by adequate and reliable corroborating evidence. Adequate and reliable corroborating evidence could not be provided for 39% of all major variances as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the reliability of the reasons for major variances.

Consistency

32. Section 41(c) of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA) requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 92% of the reported indicators were not consistent with the indicators as per the approved integrated development plan. This was due to a lack of alignment between planning and reporting documents.

Measurability

33. The FMPPI requires that the time period or deadline for delivery should be specified. A total of 100% of the targets were not time bound in specifying a time period or deadline for delivery. This was because management was not aware of the requirements of the FMPPI.
34. The FMPPI requires that indicators or measures should have clear, unambiguous data definitions so that data can be collected consistently and is easy to understand and use. A total of 100% of the indicators were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was because management was not aware of the requirements of the FMPPI.

Reliability of information

35. The FMPPPI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. The information presented with respect to basic services was not reliable when compared to the source information and evidence provided. This was due to a lack of standard operating procedures for the accurate recording of actual achievements, monitoring of the completeness of source documentation in support of actual achievements, and frequent review of the validity of reported achievements against source documentation.

Additional matter

36. I draw attention to the matter below. This matter does not have an impact on the audit findings on predetermined objectives reported above.

Material adjustments to the annual performance report

37. Material audit adjustments in the annual performance report were identified during the audit, some of which were corrected by management. Those that were not corrected are included in the basis for conclusion paragraphs.

Compliance with laws and regulations

38. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the general notice issued in terms of the PAA are as follows:

Annual financial statements, performance report and annual report

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected or the supporting records provided, which resulted in the financial statements receiving a qualified audit opinion.

Asset and liability management

40. An adequate management, accounting and information system was not in place to account for assets, as required by section 63(2)(a) of the MFMA.

Budget

41. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.
42. Quarterly reports were not submitted to the council within 30 days after the end of each quarter, as required by section 52(d) of the MFMA.

Expenditure management

- 43. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.
- 44. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Consequence management

- 45. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

Human resource management

- 46. An acting municipal manager was appointed for more than three months, in contravention of section 54A(2A) of the MSA.
- 47. Finance officials at middle management did not meet any of the prescribed competency areas, as required by Municipal Regulations on Minimum Competency Levels 8 and 9.
- 48. The municipal manager did not sign performance agreements, as required by section 57(2)(a) of the MSA.
- 49. Finance officials at middle management level did not have higher education qualifications, as required by Municipal Regulations on Minimum Competency Levels 8 and 9.

Procurement and contract management

- 50. Goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM Regulation 19(a). Deviations were not approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM Regulation 36(1).
- 51. Invitations for competitive bidding were not always advertised for the required minimum period, as required by SCM Regulation 22(1) and 22(2).
- 52. Bid adjudication was not always done by committees composed in accordance with SCM Regulation 29(2).
- 53. The prospective providers' list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualified for listing, and prospective providers were not invited to apply for such listing at least once a year, as per the requirements of SCM Regulation 14(1)(a)(ii) and 14(2).

Strategic planning and performance

54. The parent municipality did not ensure that annual performance objectives and indicators for the municipal entity were established by agreement with the municipal entity, as required by section 93B(a) of the MSA.
55. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by Municipal Planning and Performance Management Regulation 14(4)(a)(iii).
56. The internal audit unit did not audit the results of performance measurements, as required by section 45(1)(a) of the MSA and Municipal Planning and Performance Management Regulation 14(1)(a).
57. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls, as required by section 62(1)(c)(i) of the MFMA.

Internal control

58. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the qualified opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

59. Management did not exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls.
60. The municipality did not adequately review the financial statements and the annual performance report prior to their submission for auditing. Significant matters that required the adjustment of the financial statements were thus not identified and corrected.
61. The municipality did not have documented and approved internal policies and procedures to address the process of collecting, recording, processing, monitoring and reporting performance information.
62. The municipality did not implement an action plan to address the findings on performance information.

Financial and performance management

63. Management did not implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting.
64. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information. Management did not perform adequate reconciliations, as evidenced by the misstatements identified.

65. Non-compliance with laws and regulations relating to SCM and the MFMA could have been prevented had compliance been properly reviewed and monitored.

Governance

66. Management did not ensure that there was an adequately resourced and functioning internal audit unit that identified internal control deficiencies and recommended corrective action effectively.

Auditor-General

Nelspruit

30 November 2013



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence